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ASIC Enforcement Review
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

via email: ASICenforcementreview@treasury.gov.au

Dear Taskforce

Positions Paper 7: Strengthening Penalties for Corporate and Financial Sector Misconduct

Thank you for the opportunity to provide a submission on the positions paper titled 'Strengthening Penalties for Corporate and Financial Sector Misconduct' (**Paper**).

The Australian Institute of Company Directors (**AICD**) is committed to excellence in governance. We make a positive impact on society and the economy through governance education, director development and advocacy. Our, membership of more than 41,000 includes directors and senior leaders from business government and the not-for-profit sectors.

The AICD welcomes the Government's aim of ensuring that ASIC has the right tools to combat corporate and financial sector misconduct and protect consumers. The Paper provides an in-depth consideration of a number of issues which impact on the ability of ASIC to use its powers effectively. The AICD agrees with the Taskforce that it is essential that penalties are set at a level to achieve deterrence, and to ensure consistency and integrity within the regulatory regime.

The AICD supports substantial increases in penalties for a variety of offences and contraventions in the Acts.

The AICD recognises that some maximum penalties for corporate misconduct within ASIC-administered legislation no longer represent an adequate deterrent to some for wrongdoing. We acknowledge that, over time, inconsistencies have crept in to the penalty regimes in Acts administered by ASIC, causing difficulties and contradictions.

However, we have concerns about some of the proposals outlined in the Paper, including the proposed expansion of the infringement notice regime. Our responses to certain questions posed in the Positions Paper are set out in **Annexure A** to this submission.

If you would like to discuss any aspect of this submission, please contact Lysarne Pelling,

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Yours sincerely

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AUSTRALIAN INSTITUTE of COMPANY DIRECTORS

ANNEXURE A

1.	Is it appropriate that maximum terms of imprisonment for offences in ASIC-administered Acts be increased as proposed?

The AICD supports the proposed increases to maximum imprisonment terms for offences involving dishonesty or deliberate misconduct, noting the Court oversight involved.

However, in respect of the Annexure B provisions that do not involve dishonesty, such as s 952C(3), there should be no increase to these imprisonment terms as proposed, as the existing maximum terms adequately reflect the gravity of the conduct in question.

2.	Should maximum fine amounts be set by reference to a standard formula? If so, is the proposed formula appropriate?

The AICD supports the use of the proposed formula as a useful guide to determining an appropriate penalty for a particular offence. In our view, however, the formula should be amended to only permit the court to impose a penalty based on turnover in circumstances where the value of the benefits gained cannot be easily determined.

3.	Is it appropriate that the penalty for offences under section 184 of the Corporations Act be increased as proposed?

The AICD supports the proposed increase for the penalty under s 184.

4.	Is the *Peters* Test appropriate to apply to dishonesty offences across the Corporations Act?

The AICD supports the *Peters* test applying to dishonesty offences across the Corporations Act.

5.	Should imprisonment be removed from all strict and absolute liability offences in the Corporations Act (such as sections 205G and 606)?

The AICD strongly supports the removal of strict and absolute liability offences in the Corporations Act. This will ensure that imprisonment is only imposed where there is a mental element to the relevant offence, which is in accordance with good legal principle.

6.	Should all pecuniary penalties for Corporations Act other than strict and absolute liability offences have a 30 penalty unit minimum for individuals and 300 penalty unit minimum for corporate bodies?

The AICD supports the imposition of thresholds for the maximum penalties set under the Corporations Act for contraventions of offence provisions. Specifically, we support the proposals to mandate that the maximum penalty amounts set in the Corporations Act for:

- Strict and absolute liability offences should not be below 20 and 200 penalty units for individuals and corporations, respectively; and

- Offences other than strict or absolute liability offences should not be less than 30 and 300 penalty units for individuals and corporations, respectively.

That said, given the relatively serious nature of many of the offences which involve absolute or strict liability and the proposals to increase the penalties for these contraventions, the AICD

recommends that a review be undertaken to consider whether absolute or strict liability is appropriate, or whether a mental fault element should be included.

The AICD has long held the view that strict and absolute liability should be limited in its application to offences, or elements of offences, in circumstances where:

- The infraction is minor;
- The penalty for breaching the offence is small;
- There is not significant social stigma attaching to the breach; and
- Compliance does not require the exercise of significant judgment or discretion.

The AICD is concerned that a number of strict and absolute liability offences would be more appropriately classified as ordinary offences. We note that in its Inquiry into Traditional Rights and Freedoms – Encroachments by Commonwealth Laws, the Australian Law Reform Commission (**ALRC**) observed that a range of Commonwealth laws 'appear to warrant further consideration or review', including legislative provisions that provide for strict and absolute liability in corporations law and prudential and environmental regulation, for example s 588G(3).[1]

By way of example, one section worthy of review is s 588G(3) of the Corporations Act. Section 588G(3) imposes strict and absolute liability in relation to particular elements of an insolvent trading offence.[2] This feature of the offence has been criticised previously by the AICD and ASIC. For instance, ASIC observed in its submission to the ALRC Inquiry into Traditional Rights and Freedoms that:

> *This section contains what ASIC considers to be a drafting error; ASIC submits that s.588G should be amended to: (i) delete the reference to paragraph (3)(b) in paragraph (3B); and (ii) specify that the fault element for the physical element in (3)(b) is the matter stated in (3)(c). Such a reform would clarify the elements of the offence without expanding the scope of the offence or making it any easier to prove.*

The AICD agrees with ASIC that this provision requires examination and amendment.

7.	Is it appropriate to introduce the new 'ordinary' offences as outlined in Annexure C? Are there any other strict/absolute liability offences that should be complemented by an ordinary offence?

The AICD supports the introduction of these new 'ordinary' offences. However, the offences listed in Annexure C of the Paper are not minor infractions, and their breach can result in serious consequences. Indeed, as the Paper states, the currently strict liability penalty 'does not adequately reflect the importance of these obligations in maintaining consumer confidence and the integrity of the financial industry.'

In addition, many of the obligations listed in Annexure C, including obligations which relate to financial reporting and auditing obligations, are not straightforward or simple requirements. Rather, they require significant attention, deliberation, and the exercise of judgment. The AICD views strict and absolute liability to be incompatible with this complexity.

[1] Australian Law Reform Commission 2015, Traditional Rights and Freedoms – Encroachments by Commonwealth Laws, ALRC, Sydney, 23.
[2] Australian Securities and Investments Commission 2015, *ASIC Submission to ALRC Freedoms Inquiry in response to Interim Report 127.*

This being the case, the AICD suggests that the strict and absolute liability offences in Annexure C which are not of a minor nature be removed and replaced with ordinary offences.

8.	Should all Corporations Act strict and absolute liability offences be subject to the proposed penalty notice regime? Is the proposed penalty appropriate?

The AICD supports the expansion of the penalty notice regime for strict and absolute liability offences in principle.

However, we do not accept the rationale that the methodology should deviate from the AGD, which provides that an infringement/penalty notice should be 1/5th of the maximum penalty that a court could impose on a body corporate under the offence provision, but no more than 60 penalty units. The removal of imprisonment sentences for these types of offences is a welcome reform. However, it should not be used as a policy justification for deviating from the principles set out in the AGD, which have been developed with specific consideration given to their effect on body corporates.

The AICD recommends that penalty notice regime be expanded, but the penalty payable remain at 1/5th of the maximum penalty that a court could impose on a person or a body corporate.

9.	Should maximum civil penalties be set in penalty units in the Corporations Act, ASIC Act and Credit Act?

The AICD supports maximum civil penalties being set in penalty units in the Corporations Act, ASIC Act, and Credit Act.

a.	Should the maximum civil penalty for contravention of the consumer protection provisions in the ASIC Act be aligned with proposed increases to the Australian Consumer Law, although set by reference to penalty units?

It is an important legal principle that the legal consequences which flow from particular conduct should be consistent, irrespective of the particular jurisdiction or particular law which happens to apply in any given circumstance. For this reason, the AICD supports the proposed increases adopted in the Paper to achieve alignment with the proposed increases to the Australian Consumer Law (assuming that these increases will be implemented in due course).

However, as with other penalty regimes and noted in question (2) above, the AICD recommends that the court's ability to determine a penalty on the basis of turnover should only be available where the value of the benefits gained cannot be determined.

b.	Should the maximum civil penalty in the Corporations Act and Credit Act be increased as outlined above?

The AICD supports the increase proposed, subject to restricting the court's ability to determine a penalty based on turnover to circumstances where the value of any benefits gained from a breach cannot be determined.

c.	Should the maximum penalty for an individual be greater than 2,500 penalty units? If so, would $1 million (or equivalent penalty units) be an appropriate penalty

The AICD does not support increasing the maximum penalty for an individual to greater than 2,500 penalty units. The imposition of 2,500 penalty units already represents a substantial

increase in the existing penalties associated with a variety of contraventions, and a maximum penalty set at this level represents an adequate deterrent to individuals.

10.	Should the maximum penalty for an individual be the greater of a monetary amount or 3 times the benefits gained or losses avoided?

The AICD supports a fixed maximum penalty for individuals. This ensures that the penalties which apply to individuals are clear and readily ascertainable, which is important in the context of penalties imposed on natural persons.

11.	Should any provisions of the Corporations Act or Credit Act be aligned with the proposed increases to the Australian Consumer Law? In particular, should civil penalty provisions in Part 7.7A of the Corporations Act be so aligned?

The AICD supports alignment with the Australian Consumer Law for the reasons set out in our response to question 9 (a).

12.	Should ASIC be able to seek disgorgement remedies in civil penalty proceedings under the Corporations Act, ASIC Act and/or Credit Act?
13.	If so, should the making of the payment and where it is to be paid be left to the court's discretion?

As the Paper observes, valuing the loss in securities cases, and particularly in a case which involves market misconduct, can be difficult (if not impossible) to determine. In some circumstances this is likely due to the complexity of the relevant financial market in question. In other circumstances, the difficulty is caused because there may be no relevant loss to any particular party.

Against this backdrop, the AICD supports the introduction of a disgorgement remedy in civil penalty proceedings brought by ASIC under the Corporations Act, Credit Act, and ASIC Acts. It is important that the courts have adequate powers to deal with serious breaches of the law which do not result in clear or ascertainable loss or damage. The AICD also agrees that the Court should have the discretion to determine whether any payment is appropriate and how it should be applied given the circumstances.

14.	Should the Corporations Act expressly require courts to give preference to making compensation orders where a defendant does not have sufficient financial resources to pay compensation and a civil pecuniary penalty?

The AICD supports the proposal that the Corporations Act should require courts to give priority to compensation.

15.	Should the provisions in Table 6 be civil penalty provisions?

The AICD opposes the expansion of the use of civil penalty provisions in the manner suggested.

In our view, the introduction of parallel civil penalty provisions within the Corporations Act carries a risk of unjust or inconsistent outcomes, particularly with respect to the discretionary choice made by ASIC in determining whether to pursue a civil penalty provision or a criminal offence. This difficulty was observed by the ALRC in *Principled Regulation: Federal Civil and Administrative Penalties in Australia* (ALRC 95):

> *The availability of this choice can lead to uncertainty both for regulators and the regulated, and it has the potential to lead to inconsistency in the regulator's approach to commencing proceedings. Care must be taken that the reasons that a criminal prosecution is commenced against one offender while another faces 'only' civil penalty proceedings are transparent and consistent. Difficulties in proving the mental elements of the offence to the criminal standard may well be the reason for the decision to take proceedings for a civil penalty in one case, while in another, it may be that the breach lacked the requisite fault.*

For this reason, the AICD recommends a clear distinction be maintained within any ASIC-administered legislation between civil penalty provisions and criminal provisions. To the extent that the Taskforce views it as desirable to recommend that a provision becomes a civil penalty provision, we recommend that it be 'de-criminalised'.

In addition, civil penalty provisions can result in much larger financial penalties imposed on corporations when compared with criminal penalties. This could result in unintended consequences, where the criminal proceeding is both more difficult to pursue, and would yield a less desirable result from the regulator's point of view.

Finally, the AICD believes that the procedural protections afforded to individuals within the context of criminal proceedings are an important safeguard which should be maintained and not diluted.

For these reasons, the AICD recommends that the provisions in Table 6 be either criminal provisions, or civil penalty provisions, but not both.

16. Should there be an express provision stating that where the fault elements of a provision and/or the default fault elements in the Criminal Code can be established the relevant contravention is a criminal offence?

The AICD is strongly opposed to this proposal. The AICD is particularly concerned that this proposal will cause significant uncertainty within the law for the reasons stated in our response to question 15. In addition, the AICD is concerned that such a change risks diluting or destroying procedural protections which are usually afforded a person in a criminal prosecution.

17. Should any of the provisions in Table 7 be civil penalty provisions?

18. Should any other provisions of ASIC-administered Acts be civil penalty provisions?

See our response to question 15.

19. Should section 180 of the Corporations Act be a civil penalty provision?

The AICD supports amending s 1317E to remove the statutory negligence provisions ss 180 and 601FD(1)(b) from the civil penalty regime.

The civil penalty regime was introduced in 1993 in response to concerns that the existing criminal penalty regime applying to directors' duties was unsatisfactory. A key deficiency was the application of criminal sanctions for misconduct that was not 'genuinely criminal in nature', that is, fraudulent or dishonest conduct.[3] To address this deficiency the corporations law was

[3] Senate Standing Committee on Legal and Constitutional Affairs, Parliament of Australia, *Company Directors' Duties: Report on the Social and Fiduciary Duties and Obligations of Company Directors* (1989) at [13.12].

amended to deem officers' general duties – including the statutory duty of care and diligence – to be civil penalty provisions,[4] with criminal sanctions only applying for contraventions that were made dishonestly or fraudulently.[5] The decision to introduce the civil penalty regime in 1993 does not appear to have considered the appropriateness of the regime's application to the statutory duty of care and diligence.

Nor does this issue appear to have been deliberated when the statutory duty of care and diligence was subsequently decriminalised under the *Corporate Law Reform Economic Program Act 1999* (Cth) on the basis that the 'concept of negligence is inconsistent with dishonesty'.[6]

The AICD welcomes the Government's consultation on this important issue as part of the Taskforce's penalties review.

Civil penalty provisions are a 'hybrid between,'[7] or 'lie somewhere between,'[8] the criminal and civil law. They are intended to prevent or punish public harm,[9] and have been characterised as 'punitive civil sanctions'.[10] It is the AICD's strong view that it is inappropriate for ordinary negligence, which is not predicated on conscious wrongdoing, to attract punitive pecuniary penalties (payable to the regulator on the Commonwealth's behalf) or disqualification orders. Instead, ordinary negligence – whether statutory or general law – should give rise to a right to compensatory remedies for losses suffered.

In addition to our policy concern regarding the appropriateness of statutory negligence attracting civil penalty sanctions, this issue needs to be considered in light of the regulator's 'stepping stone' approach to prosecuting officers for breaches of s 180. Under this approach, the regulator alleges that s 180 has been breached due to the officers' failure to prevent a corporate contravention. This enforcement approach compounds the unfairness of a breach of s 180 giving rise to a civil penalty. The stepping stones approach circumvents the accessorial liability provisions of the Corporations Act, which require the regulator to prove that the officers were 'involved' in the corporation contravention. By not needing to prove the officers' 'involvement' in the breach, the officers are deprived of any defences to accessorial liability that might otherwise have been available in the circumstances.

Also, the stepping stones approach to s 180 may result in the officers suffering harsher consequences for a corporate breach than the primary offender, being the company itself. This outcome can arise because, unlike s 180, the company's contravention may not constitute a breach of a civil penalty provision or attract any penalties. As Bednall & Hanrahan have stated: 'the consequences of a form of derivative liability should not be more harsh than the consequences of the primary contravention. To hold otherwise is disproportionate, and therefore unjust'.[11]

The inappropriateness for s 180(1) to remain a civil penalty provision is further exacerbated by the limited operation of the statutory business judgment rule. As the courts have confirmed,

[4] Subsections 232(4) and 1317DA of the Corporations Law.
[5] Subsection 1317FA(1) of the Corporations Law.
[6] Explanatory Memorandum, Corporate Law Economic Reform Bill 1992 at [6.1]
[7] Australian Law Reform Commission, *Principled Regulation: Federal Civil and Administrative Penalties in Australia*, Report No 95 (2003) (**ALRC Report 95**) at [2.47].
[8] Austin RP and Ramsay I M, *Ford, Austin and Ramsay's Principles of Corporations Law*, LexisNexis Butterworths, Australia, 16th edition, 2015 at 99.
[9] ALRC Report at [2.47].
[10] ALRC Report at [2.48] citing Mann K *Punitive Civil Sanctions: The Middleground Between Criminal and Civil Law* (1992) 101(5) Yale Law Journal 1795 at 1798.
[11] Bednall T and Hanrahan P *Officers' liability for mandatory corporate disclosure: Two paths, two destinations?* (2013) 31 C&SLJ 474 at 498.

ss 180(2) and (3) do not apply to judgments that are administrative or compliance-based in nature.[12] With such a limited defence, it is unjust that an officer can be subject to a civil penalty provision for ordinary negligence.

Further, the AICD has had the benefit of considering the submission of the Corporations Committee of the Business Law Section of the Law Council on this issue and endorse the Committee's analysis.

22.	Which current and new civil penalty provisions are suitable for infringement notices (see Annexure D)?

The AICD strongly opposes the expansion of the infringement notice regime. The AICD agrees with the positions stated previously by the Law Council of Australia and the ALRC. The imposition of infringement notices is a form of lazy regulation, and undermines the credibility and transparency of regulatory action. ASIC should be sufficiently resourced and equipped to pursue these contraventions through the Courts. The Court have a critical role to play in the proper functioning of the corporate regulatory system.

In any event, the AICD is concerned that the vast majority of the contraventions listed in Annexure D would not fall within the AGD Guidelines for the application of infringement notices. The AGD Guidelines provide the following:

> *An infringement notice scheme may be employed for relatively minor offences, where a high volume of contraventions is expected, and where a penalty must be imposed immediately to be effective. The offences should be such that an enforcement officer can easily make an assessment of guilt or innocence. An infringement notice scheme should generally only apply to strict or absolute liability offences.*

The AICD notes the following in relation to the contraventions in Annexure D:

- With the exception of s 188(1) and (2), the contraventions listed in Annexure D are not relatively minor offences, but relatively serious offences.
- It is not apparent, in relation to any of the offences listed in Annexure D, that a penalty needs to be imposed immediately to be effective.
- A number of offences listed in Annexure D would be relatively difficult or complex to make an assessment of guilt or innocence. In particular (but not limited to), ss 205G, 344(1), 601FC(5), 606, 670A, 674(2A), 671B, 675(2A), 728, 792A, 821A, 904A 961K(1) and (2), 912A, 912D, 961L, and 952E of the Corporations Act.

For these reasons, the AICD recommends against the expansion of the infringement notice regime to any of the provisions listed in Annexure D.

[12] See, for example, *ASIC v Fortescue Metals Group* (2011) 190 FCR 364 at 427.